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How Do Western Companies Respond to the Opening of Central and East European Economies? Survey Evidence From a Small Open Economy - Belgium

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I. INTRODUCTION

In almost all post-communist countries widespread economic reforms have taken place and an increasingly growing private sector has been established. Furthermore, increased trade flows between the West and the East emerged as a consequence of the opening up of Central and Eastern Europe. Most of the transition countries are now starting to emerge from their deep recessions and show in fact high and positive growth of which many Western nations can only dream. Real GDP in Poland, Hungary and the Czech Republic for instance grew at respectively 7.0%, 1.5% and 4.8% in 1995 (EBRD (1996)). However, at the same time fear has grown in the industrialised countries that the increased globalisation of the economy and especially the increased competition from Central and Eastern Europe will harm domestic industry and welfare[1]. Wood (1995) argues that the deteriorating situation of unskilled workers in developed countries is caused mainly by

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an expansion of trade with developing countries, while Krugman and Lawrence (1994) argue that the effects of trade have been relatively small. Yet, little is known about the empirical contents of such claims and in particular about the effects on firm behaviour of trade liberalisation with Central and Eastern Europe. From a theoretical point of view integration of Central and Eastern Europe (CEE) with the West can be achieved via various channels. First, workers in search of better paid jobs will want to move to the West. However, as this is not easily achieved (due to EU legislation and cultural factors) there will be an increased mobility of capital and/or goods. The latter would be reflected in an increased volume of trade, the former in more FDI that could be associated with a reduction of jobs in the Western home based firm.

The purpose of this paper is to investigate those dimensions. In particular, we discuss the results of a large-scale survey of Belgian companies that invested and/or exported to Central and Eastern Europe. In addition we merged the survey data with the published company accounts of the sampled firms which allowed us to make use of both qualitative data not readily available in published company accounts and quantitative data such as employment, wages, turnover, etc.. Since Belgium is a small open economy the results in this paper are particularly relevant for most European small open countries such as the Netherlands, Austria, etc.. Only a few papers exist dealing with similar issues and most of them focus on aspects of foreign direct investment (FDI). Genco, Taurelli and Viezolli (1993) report survey results of a sample of 82 companies in France, Germany, the UK and Italy that invested in CEE and their focus was predominantly on motivation for investments. Meyer (1995) reports results of a survey of 268 companies in Germany and the UK and looks for patterns and explanations of FDI in CEE. Gabriel, Benito and Welch (1994) conducted a survey with Norwegian companies investigating the involvement of Norwegian firms in Eastern Europe. They also reported on the plans and expectations of these companies with regard to business in a changing economic environment of Eastern Europe.

The paper is organised as follows. In section II we discuss the sample framework, the design of the questionnaire and the basic sample characteristics, while section III reports the main results of the survey. The increased competition from low-wage countries is often seen as one of the causes of increased unemployment in the West. In sec-

tion IV we focus on the effects of increased globalisation on employment determination.

II. SAMPLE FRAMEWORK

In July-August 1996, we sent out 1580 questionnaires, covering issues related to competition, industrial relations, marketing, and economic activities in CEE. The Belgian Foreign Trade Board provided us with a list of all companies that exported and/or invested in Central and Eastern Europe.

Following a pilot study with a Belgian multinational active in CEE, we conducted a postal survey for which we selected companies at random regardless of firm size or sector; 312 companies replied (i.e. 20%), 281 of which could be used for the analysis. We subsequently merged our survey data with company accounts data from the Central Bank of Belgium. We were able to match 262 companies, the remainder are typically small companies employing no people[2]. The firms are divided across most one digit NACE sectors, as can be seen in Table 1.

TABLE 1

Firms in Sample, by Sector

Sector	Percentage of firms in sample
Agriculture (NACE 0)	1.5 %
Extraction / Processing of non-energetic production materials (NACE 22, 23, 24)	2.6 %
Chemical industry (NACE 25)	9.1 %
Manufacturing (NACE 3, 4)	47 %
Construction (NACE 5)	3.4 %
Wholesale (NACE 61)	20 %
Commercial sector, except wholesale (NACE 63 - 67)	3.0 %
Transport, communication and services (NACE 7,8,9)	14.1 %

Most companies belong to the manufacturing industries and the commercial sector. Especially food drink and tobacco, textiles, the chemical industry, wholesale and service related sectors are well represented. The high proportion of wholesale companies should not be a surprise as many of the companies currently exporting to the CEE are import/export businesses acting as intermediaries and not actually producing anything themselves. This is typical for trade with newly emerging markets.

III. MAIN RESULTS

In this section we provide summary statistics on the responses of the survey. This section is divided into two parts, the first deals with competition in an international environment, the second concentrates specifically on production in Central and Eastern Europe.

A. *Competition*

In order to obtain an idea of the extent of globalisation, we asked how many competitors the company faces and how the degree of competition evolves over 2 different periods. The periods considered (1986-1989/1990-1995) coincide more or less with the pre- and post- transition periods in Central and Eastern Europe. In addition we made a distinction between changes in domestic competition and foreign competition. Furthermore if the company indicated that the degree of competition increased, we asked to rank some of the reasons for this increase, also giving them the possibility to add their own reasons.

As can be seen in Table 2, most companies or 72% operated in a competitive environment, at least if we measure competitiveness by the number of rivals a firm is facing.

TABLE 2

Number of Competitors of Firms in Sample

Number of Competitors	Percentage of Firms
No Competitors	1, 4%
Between 1 and 5	26%
More than 5	72%

When we asked about *changes* in competition, only a few firms reported a reduction in competition. In the period 1986-89 only 39%, resp. 51% of the firms experienced an increase in domestic resp. foreign competition, while in the period 1990-95 this increased to 54% respectively 81% (Table 3). Especially the increase in foreign competition for the post-communist years is striking.

TABLE 3

Experienced Change in Foreign Competition

	1986-1989		
	increase	no change	decrease
Domestic	39%	55 %	6%
Foreign	51%	45 %	3%
	1990-1995		
	increase	nochange	decrease
Domestic	54%	37 %	9%
Foreing	81	16 %	3%

(missing cases are excluded from the calculations)

In Table 4 we summarise the importance attached to some of the possible causes for increased foreign competition.

TABLE 4

Causes of Increase in Foreign Competition

Increase in Foreign Competition due to...	Rank 1	Rank 2	Rank 3
Labour Costs	49%	16%	6%
Other Reasons	21%	6%	4%
Globalisation	18%	15%	11%
Product Innovation	16%	14%	19%
Technological Developments	16%	12%	18%

Note:

* Rank 1 is the more important, rank 3 is less important. (options were ranked from 1 to 5).
* Columns do not sum to a 100% since the same rank to multiple options was allowed.
* The percentages refer to 209 companies that experienced an increase in foreign competition during the period 1990-1995.

Almost half of the respondents consider the lower labour costs abroad to be the most important factor contributing to the increase in foreign competition during the 1990-1995 period. It is well known that, due to a number of institutional restrictions, labour costs in Belgium are very high. The gross labour cost for an employer is on average twice the net take-home pay. Especially for companies operating in international sectors the regulatory nature of the Belgian labour market seems to be a plausible explanation for the importance of labour costs in Table 4. This is also consistent with recent micro-econometric evidence estimating a long run labour elasticity of well above 1 in absolute value for Belgium (Konings and Roodhooft (1997)). An-

other striking element which is not immediately visible from the table is that one of the most frequently mentioned "other reasons" for increased foreign competition was the overvalued exchange rate of the Belgian frank.

While labour costs seem to be an important factor for explaining increased foreign competition, this does not imply it is mainly caused by competition from low-wage countries. We also asked to rank the regions from where the increase in foreign competition originated. Tables 5a and 5b clearly show that the rise in competition mainly originated from the Western countries for both the pre- and post-transition periods.

TABLE 5A

Regions of origin of increase in Foreign Competition (1986-1989)

Region	Rank 1	Rank 2	Rank 3
Western Countries (*)	79%	8%	6%
Central and Eastern Europe	6%	18%	20%
South-East Asia	15%	20%	19%
Others (**)	9%	9%	7%

(*) Western Europe, USA, Canada, Australia
(**) e.g. Latin-America, Turkey, Middle-East, Africa

TABLE 5B

Regions of origin of increase in Foreign Competition (1990-1995)

Region	Rank 1	Rank 2	Rank 3
Western Countries (*)	66%	11%	9%
Central and Eastern Europe	17%	26%	15%
South-East Asia	20%	19%	18%
Others (**)	9%	7%	9%

(*) Western Europe, USA, Canada, Australia
(**) e.g. Latin-America, Turkey, Middle-East, Africa

The comparatively low impact of competition from CEE is not surprising given the limited trade flows with Central and Eastern Europe at this stage. For instance in 1992, only 1.39% of BLEU[3] exports went to CEE, while 73.9% went to the EU. 1.66 % of total imports originated from CEE compared to 74.6% from the EU (source: Belgian Foreign Trade Board). However, an important evolution may be detected on inspection of Table 5b.

In the second period, 17% (26%) of the companies ranked CEE as the first (second) source of competitive pressure, up from 6% (16%) in the first period. Although SEA's importance remains greater in either period and also increased over time, its rise as a prime source of competition was far less marked than CEE's. Thus, while Western competitors are still the most relevant ones, there is a clear trend towards increasing competition from both the South-East Asian and especially from the CEE countries. This trend can be expected to go on given the growth potential of most of the CEE countries.

B. *Production in Central and Eastern Europe*

16 % of the firms in our sample have their own production, service or sales facilities in Central-and Eastern Europe. Most of them are situated in the more advanced and politically stable countries of Central Europe and in Russia. Of the 46 companies with production facilities in CEE only 18 have transferred production lines from Belgium to CEE and only 2 firms admitted that this coincided with a decrease in the domestic workforce. When we asked for the reasons that companies delocalised their activities to CEE, the most important reasons they gave were labour costs and expansion arguments, while general restructuring and social legislation were not important.

While labour costs seem to matter, it is important to view this argument jointly with productivity. If productivity is lower in CEE it is not necessarily an advantage that labour costs are lower, it just reflects the lower productivity. Indeed, as shown in Table 6, 73% or 35 companies with production facilities in CEE find that productivity is lower or much lower than in the home country. 21 of them indicate cultural background and work ethics as the principal cause. Aged technology and a less qualified workforce also play a role. Trade unions, although politically important in many of the CEE countries, do not seem to influence productivity in an adverse way.

TABLE 6

Productivity of CEE production facility compared to its Belgian counterpart

Relative Productivity in CEE	Percentage
Much Lower	23 %
Lower	50 %
Equal	19 %
Higher	6 %
Much Higher	2 %

We finally asked a series of questions related to risk factors for investment in CEE. We asked to rank the five most important risk factors for investing in CEE, out of a list of 12 possible risk factors, leaving the option of adding one more risk factor to the list. We asked this question to the companies that invested in CEE, as well as to those who did not invest or plan to invest. The results are summarised in Table 7.

TABLE 7

Risk factors for investing in CEE

Risk Factors.	Rank 1	Rank 2	Rank 3
Lack of clear legislation	25 %	12 %	9 %
Political instability	19 %	14 %	7 %
Uncertainty about the currency value	18 %	11 %	7 %
Insufficiently developed market economy	15 %	8 %	10 %
Difficulties in obtaining management control	13 %	7 %	10 %
Insufficiently developed capital market	11 %	7 %	8 %
Deficient infrastructure	11 %	8 %	13 %
Lack of market information	9 %	6 %	5 %
Aged production technology	8 %	4 %	7 %
Other Risk Factors	8 %	2 %	1 %
Lack of protection of property rights	7 %	7 %	7 %
Uncertainty about price fluctuations	7 %	5 %	5 %
Lack of protection of intellectual rights	6 %	2 %	4 %

Table 7 shows that many companies still consider the market economies of CEE to be underdeveloped, with a lack of clear legislation. Furthermore political instability and the unstable currencies are important risk factors. This is consistent with the findings of Genco, Taurelli and Viezolli (1993) covering 83 companies. They found that the main risk factors relate to the weakness of the legislative framework, with the strictly economic problems coming only second.

There are also difficulties in obtaining control over the management when acquiring CEE companies. This is an important observation which fits with the fact that most privatised companies in CEE do not perform significantly better than their state owned counterparts, while the newly established or *de novo* private firms consistently perform better as shown in Konings, Lehmann and Schaffer (1996). A plausible explanation for this is that old management is still in place and therefore old management methods will not change performance.

Among the category "other risk factors" it was often reported that chaos and mafia practices, which all add to the uncertainty, are important risk factors.

Despite those risks, companies do or are planning to invest in CEE. Table 8 shows the reasons why. We listed 5 reasons to invest, gave the option of adding a sixth one and then asked to rank them from 1 to 6. 204 companies answered this question.

TABLE 8

Reasons to Invest in CEE

Reason to Invest.	Rank 1	Rank 2	Rank 3
Explore new markets	43%	25%	11%
Achieve a strategically position on these markets	37%	25%	16%
Making use of cheaper labour	26%	14%	19%
Making use of the fiscal advantages	2%	6%	10%
Expect target country to enter EU	7%	5%	11%
Other Reasons	2%	0%	2%

Note: multiple reasons could obtain the same rank number, this explains why the columns do not need to sum to 100%.

Despite the importance of labour costs as one of the causes of increased foreign competition for Belgian companies (Table 4), making use of cheap labour as a reason for investment is only given by 26% of the companies as most important reason. Especially the exploration of new markets and the achievement of a strategic position is given often as the most important reason for investment. This suggests that companies are willing to invest not for the immediate short run profits but rather to have a first-mover advantage, i.e. to obtain a competitive advantage over newcomers that get on the market at a later stage.

From the above results it is clear that most firms experienced increased globalisation, either in the form of increased foreign competition, or in terms of a direct investment which in a few cases implied delocalising some of the activities to Central and Eastern Europe. While labour costs seem to matter, also other factors (such as expansion incentives and an overvalued exchange rate) are important elements in the process of globalisation. A lot of the recent debate has focused on the effects of increased globalisation on jobs. It is this issue that we take up in the next section.

IV. GLOBALISATION AND JOBS

In this section we focus on globalisation and in particular on the effects of increased foreign competition on the demand for labour in Belgian export oriented enterprises. Fear has grown in the industrialised countries that free trade with low-wage developing countries and especially with Central and East European countries will harm domestic industry and employment[4]. This is particularly relevant for small open economies that are constantly exposed to international competitive pressure and high and rigid wages are sometimes blamed for causing high unemployment through trade (Wood (1995)).

From a theoretical perspective there are several models that lead to different predictions concerning the effects of free trade on jobs and wages. In the traditional constant-returns-to-scale framework the Stolper-Samuelson (1941) theorem argues that North-South trade will lower wages in the North while raising wages in the South. In the North, jobs will be created in the capital intensive sector and destroyed in the labour intensive ones. In equilibrium job creation and destruction must cancel out leaving net employment unchanged after free trade. International trade theory has developed substantially since the Stolper-Samuelson theorem. In particular, it turns out that a substantial fraction of trade is North-North intra-industry trade, which led to the development of models with increasing returns to scale (e.g. Panagarya (1980); Helpman and Krugman (1985)). These models show that intra-industry trade can have positive effects on wages and employment. All in all the predictions that come from international trade theory can be summarised as follows: Increased economic integration should lead to workers migrating to the high wage regions in search for better paid jobs. As labour mobility is restricted (by law and cultural differences) the economic response is via increased trade in

goods and/or increased capital mobility. The latter can be foreign direct investment, possibly involving delocalisation of production facilities, which has implications for the employment level and structure in the home country.

Empirically there is no consensus on the effects of globalisation and jobs. Grossman (1986) analyses the effect of import competition on US employment in the steel sector, but fails to find any significant effect of import competition other than the one caused by the appreciation of the dollar and the secular decline of the steel industry. Revenga (1992) uses industry-level panel data for the US manufacturing industries in the period 1980-85 and reports negative and significant effects of import competition on employment and wages. Konings and Vandenbussche (1995) estimate a structural labour demand equation on UK firm-level panel data between 1982-89 and find no overall effect of increased foreign competition on employment, but a positive effect on wages. The effects vary depending on the manufacturing vs. non-manufacturing sector, the degree of unionisation and competition firms face.

Also foreign direct investment and outsourcing affects employment. There is a direct effect of employment removal in case foreign production simply replaces domestic production. Indirect mitigating effects occur as a result of increased exports of supplies, an increase in management staff at home, and as a result of company growth after obtaining a better competitive position through cost reductions.

Empirically, Feenstra and Hanson (1996), find a negative effect of outsourcing on relative labour demand for the low-skilled in the US for the 1979-1990 period. US surveys, however, show that the overall employment effect of delocalisation on employment is positive (see e.g. Mucchielli (1994)). The positive effect is accounted for by the export stimulation effect and increasing employment at the home office and at supporting firms.

In what follows we will be using information drawn from the individual company accounts jointly with the collected survey material on increased foreign competition to estimate the effects of foreign competition on domestic labour demand. We have information on employment, average wages, capital and output for 263 companies of our sample over the period 1990-95. In Table 3 of section 3 it can be seen that 81% of the companies experienced an increase in foreign competition over that period.

To obtain a testable employment equation, consider a general production function,

$$Q=F(L,K) \tag{1}$$

where Q stands for output, L for labour and K for capital. The unconditional demand for labour has the general form of:

$$L=v(w,r,p,), \tag{2}$$

where w is the unit wage cost, r is the unit capital cost and p is the product price firms face. The price that firms face is exogenously given in the case of perfect competition; however, in the more likely case of imperfect competition (or increasing returns to scale) this price reflects the degree of competition that (oligopolistic) firms are facing. Under the assumption of imperfect competition it is well known that the optimal price will be above the price under perfect competition which implies lower output levels and therefore lower employment levels. There are several ways to model price behaviour, ranging from joint profit maximisation to Bertrand competition. Instead of specifying a specific oligopoly model and since prices are not observable we look for empirical proxies that will affect prices, or

$$p=g(Q,c,fc,inv) \tag{3}$$

Apart from the dependence of price on output[5], prices will be affected by c reflecting the number of competitors firms are facing (a dummy equal to 1 if the firm faces more than 5 competitors), fc stands for changing international competition (a dummy equal to 1 if the firm experienced an increase in international competition over the period 1990-95) and inv stands for investment activities in Central and Eastern Europe (a dummy equal to 1 if the firm has any production facilities in Central and Eastern Europe). The number of rivals a firm is facing should have a negative effect on prices and therefore a positive effect on the demand for labour in the industry because the competitive outcome is approached. At the firm-level the outcome is ambiguous. If more firms enter the market, product demand and thus also labour demand will be shared among more firms, leading to a reduction in employment at the firm level. However, if we take into account that the market expands as well, which is clearly the case when

we consider CEE, labour demand is also likely to expand. Similarly, an increase in foreign competition should reduce prices, thereby reducing domestic firms' market power. This is the so-called "imports-as-market-discipline" hypothesis which has been tested and confirmed by Levinsohn (1993) on the basis of Turkish firm level data. Thus it is expected that increased foreign competition lowers prices and therefore increases the demand for labour. Finally, if the firm has production facilities in Central and Eastern Europe it can benefit from lower production costs which enables the firm to improve its competitive position vis-à-vis its competitors, and win market share in the long run. This suggests that prices should fall as the firm has invested in CEE, hence employment should rise.

Combining (2) and (3) and specifying a log linear approximation of a labour demand function we obtain a testable employment equation,

$$\ln L_{it} = \alpha_0 + \alpha_1 \ln w_{it} + \alpha_2 \ln Q_{it} + \alpha_3 c_i + \alpha_4 fc_i + \alpha_5 inv + \epsilon_{it} \qquad (4)$$

where ln stands for natural logarithm, subscript i and t denote resp. firm and time and ϵ is an error term which needs some more explanation. Since we are using panel data it is possible to take into account firm heterogeneity. Specifically, assume that

$$\epsilon_{it} = \nu_i + \vartheta_{it}$$

with

$$E(\vartheta^2_{it}) = \sigma_\vartheta^2$$
$$E(\nu^2_i) = \sigma^2_\nu$$
$$E(\vartheta_{it}\vartheta_{sj}) = 0$$
$$E(\nu_i \nu_j) = 0$$

Thus we model firm heterogeneity by an unobservable firm-specific random effect, ν_i. This type of models are referred to as random effects models and we estimate (4) using General Least Squares where we take into account the above assumptions (Greene (1990), pp. 470-71).

Notice that we did not specify the user cost of capital in equation (4). This is because we do not observe this at the firm level. However, assuming perfect capital markets firms will have access to capital at the same price, so it should only fluctuate over time. In our regressions we included time dummies to control for this, but also for other non-observable aggregate shocks[6]. We also experimented with including the capital stock as one of the explanatory variables.

In column (1) of Table 9 we report the estimates for equation (4), while in column (2) we also included the log of the capital stock as one of the explanatory variables. The number of rivals does not have a statistically significant effect on the demand for labour, although it is estimated with a positive coefficient. Increased foreign competition has a positive and significant effect on employment, which is over and above the wage effect. This is consistent with the theory, assuming market expansion takes place. This assumption is shown to be valid by our survey findings. Thus this suggests that increased globalisation is a good thing for the demand for labour and actually increases it[7]. Also, firms that have production facilities in Central and Eastern Europe have a significantly higher employment level than those that do not have production facilities in transition countries[8]. The results of increased foreign competition are quite strong. It is important to note that our sample, due to the sample selection, consists of firms that operate in an international environment. The effects for domestic firms that operate predominantly on the domestic market may be different, probably depending on their ability to adjust to external shocks. Nevertheless, the results reported here suggest that at least for a small open economy where presumably most firms deal in an international market increased foreign competition enhances job creation.

TABLE 9

Dependent Variable: ln(L):
Random Effects GLS Estimation

	(1)	(2)	(3)	(4)	(5)
ln(w)	-0.575* (0.045)	-0.581* (0.042)	-0.581* (0.042)	-0.442* (0.072)	-0.579* (0.042)
ln(Q)	0.499* (0.019)	0.507* (0.021)	0.507* (0.021)	–	0.509* (0.020)
$\ln(Q_{t-1})$	–	–	–	0.143* (0.024)	–
ln(K)	–	0.155* (0.014)	0.155* (0.014)	0.339* (0.020)	0.154* (0.014)
c	0.157 (0.160)	0.057 (0.131)	-0.065 (0.258)	0.150 (0.171)	0.084 (0.131)
fc	0.435* (0.174)	0.327* (0.143)	0.221 (0.239)	0.415* (0.180)	0.317* (0.143)
*c*fc*	–	–	0.164 (0.298)	–	–
inv	0.354**(0.187)	0.285** (0.154)	0.290** (0.154)	0.413* (0.198)	–
number of firms in estimation	214	213	213	194	213
Overall R-sq	0.74	0.82	0.82	0.78	0.82

Note:
1. all equations include time dummies, standard errors in brackets.
2. * significant at the significant at the 5% level, ** significant at the 10% level
3. Q and w have been normalised on a 12-month accounting year

How robust are the above results? If the mechanism underlying the positive effect on jobs is the "disciplining" effect of foreign competition on price behaviour, then we would expect to find that the effect of foreign competition should especially be present in those industries that are relatively concentrated. We therefore interacted c, the number of rivals a firm is facing with fc, the dummy indicating whether the firm experienced an increase in foreign competition. In column (3) we show the results. The coefficient of c, fc and the interaction term become insignificant. This is probably due to the high multicollinearity between c and c*fc, as well as between fc and c*fc. The other estimated coefficients remain the same.

A second concern with the above regressions is related to potential endogeneity of especially output and the investment dummy, inv. The reason why we included output in the regression is to control for "demand" shocks. As all firms in the sample are operating in the international market, this can also be seen as a proxy for international demand (or exports) shocks, hence it is not unreasonable to assume it is exogenous. Yet, we experimented with including lagged output, rather than current output. This avoids a potential simultaneity bias. As can be seen in column (4) the coefficients still have the same sign and in fact the magnitude of the effect of foreign competition becomes stronger now. The potential endogeneity of investment comes from the hypothesis that the larger firms are more likely to invest. However, in the case of investment in Central and Eastern Europe both small and large firms in our sample have production facilities in CEE. This is because relatively small trading and service firms, as well as large multinationals invest in CEE. This is illustrated in Table 10. Although firms with more than a hundred employees seem to be more likely to have production facilities in CEE, the Pearson chi2 statistic for independence of rows and columns does not allow us to reject that firm size is independent of the decision to produce in CEE.

TABLE 10

Number of Investors by Firm Size

Number of Employees (1995)	Non-Investors	Investors	Total
1-19	64 (89 %)	8 (11 %)	72 (100 %)
20-49	37 (84 %)	7 (16 %)	44 (100 %)
50-100	31 (86 %)	5 (14 %)	36 (100 %)
100 +	48 (77 %)	14 (23 %)	62 (100 %)
Total	180 (84 %)	34 (16 %)	214 (100 %)

Pearson chi2 (3) = 3.4152 Pr. 0.332

We also experimented with leaving inv out of the regression; the coefficients on fc, as well as the others stayed the same, as shown in column (5) of Table 9.

V. CONCLUSION

It is of important policy concern to assess to what extent the increased unemployment in the European Union is driven by increased globalisation and increased foreign competition from low wage countries, in particular. This paper takes up this question in the context of the opening of Central and Eastern Europe. To investigate company behaviour in response to the opening of Central and Eastern Europe we report a large scale survey of Belgian enterprises that invested and/or exported in Central and Eastern Europe. We found that surprisingly few companies delocalised their production facilities to the region, but a substantial number of companies do have production facilities or have contractual links with companies in Central and Eastern Europe. Especially the exploration of new markets and the achievement of a strategic position in these markets turn out to be important driving forces for investment in CEE, while cheap labour is less important. Important risk factors for investing in CEE are especially related to the lack of a clear legislation and ill-defined property rights. Another finding is that globalisation is a real phenomenon. While in the period 1986-90 only 51% of the companies in the sample experienced increased foreign competition, this fraction increased to 81%

after 1990. While South-East Asia and Central and Eastern Europe gain in importance, other Western regions remain the prime source of competition. High labour costs and an overvalued Belgian franc are often given as the most important factors causing this increase in foreign competition. We then test whether globalisation was good or bad for jobs. We find strong evidence that an increase in foreign competition leads to more jobs in the West. This can be explained by the efficiency-enhancing effects foreign competition exerts, with the market expanding at the same time. We also found that firms that have production facilities in CEE have higher labour demand (although the direction of the causation has not been fully established). This could be related to risk diversification, the ability to produce cheaper and hence to price more competitively in the domestic market, and access to new markets which may lead to growth in the domestic firm as well.

NOTES

1. Bhagwati (1994) in a recent survey article discusses nicely the current concern about free trade and competition from the "South". The 1995 summer edition of the Journal of Economic Perspectives published a symposium on this issue.
2. An increasing number of companies switch from employing workers to working with independent "entrepreneurs" to avoid the payment of high employer contributions.
3. Belgium-Luxembourg Economic Union.
4. For a survey of the issues see Janssens (1997) or Wes (1996).
5. One of the problems in measuring output is that theoretically we should use a quantity indicator (e.g. number of products sold) instead of a value indicator (e.g. value-added or sales). However, this is not feasible in practice because we do not have data on prices and quantities separately. An additional problem is that controlling for Q is hard to interpret across industries.
6. The time dummies also solve the potential statistic problems associated with the likely non-stationarity of the series w, Q and L.
7. We also experimented with a wage equation. After controlling for output and capital we found that increased foreign competition had a weak negative effect on average wages.
8. We are aware that causation could run in both ways here.

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